NOTES

CURRENCY: THE PROBLEM OF FLEXIBILITY

There seems to be a general agreement of opinion, both among the economists and among the men engaged in active banking, that, in spite of the currency legislation of the past two years, the currency system of the country is still in need of substantial reform, and that flexibility, the power to expand and contract in response to the varying needs of the business world, is the one desirable quality to be given at the present time. The question has already been discussed to a considerable extent by members of Congress, in newspapers and magazines, and at various meetings of state and national bankers' associations. But while there is practical unanimity as to the thing to be desired, there is considerable diversity of opinion as to the means of attaining it. Perhaps the most prominent programme that has yet been brought forward is that of providing for the issuance, either through the national banks or through a central bank of issue, of a sort of emergency currency in the form of bank-notes redeemable within a given period of time. Many of the writers and speakers on the subject regard this plan as the easiest and most expeditious solution of the difficulty; many others, however, look upon it as an objectionable and somewhat dangerous expedient, likely to fail of its purpose in the time of greatest need.

The objections to the plan are based chiefly upon the contention that a widely fluctuating volume of bank-notes is not a remedy for an over-extended credit situation, bringing about an unhealthy, if not a dangerous, proportion of credits to the country's basic money, and that, although the issuance of bank-notes may afford relief so far as mere volume of currency is concerned, it also has the undesirable effect of producing a still greater disproportion of the aggregate liabilities of the banks of the country to the total volume of gold and silver.

No one will contest the point that a widely fluctuating quantity of bank-notes is not a remedy for an over-extended credit situation. When the bow of credit has been stretched to the breaking-point, it is useless to talk about relieving the difficulty by a

still further expansion of credit. There can be no remedy for a situation of this kind except to call a halt in the extension of such credit and to return to the practice of sound banking. But the reason for opposing the issuance of bank-notes in times of financial stringency, namely, that they would bring about an unhealthy proportion of credits to the country's basic money, shows a false conception both of what is meant by the term, the country's basic money, and of the relation which the latter bears to our general currency.

Basic, or standard, money is, in its narrower sense, that portion of our currency manufactured from the commodity which serves as the standard of value—that is, from gold. Its functions, too, as a standard of value and as a medium of exchange, are quite distinct. In the former use it serves simply as the standard in measuring and expressing the values of other commodities; in the latter it becomes only one small element in a complex system of currency created and used for the purpose of facilitating exchange. Indeed, one can conceive of a perfectly useful and legitimate standard of value which might never be coined into money at all; and how small a proportion the so-called standard money under the present system bears to the rest of the currency of the country can be seen by a very simple comparison. The total amount of actual money in the United States at the present time is, approximately,[1] $3,406,611,791, divided as follows: gold coin and bullion in the Treasury (including the fund for the redemption of gold and silver certificates), $1,644,900,733; "standard" silver dollars, $563,985,812; subsidiary silver, $158,587,115; Treasury notes of 1890, $4,274,000; United States notes, $346,618,016; national-bank notes, $688,183,115. Deducting from the original total the $1,644,900,733 in gold and the $150,000,000 worth of United States notes which are covered by actual gold reserve, we find that $1,611,711,058 of this total, or more than 47 per cent., is in reality credit currency based upon the government's promise to pay. Of the total general stock given above, $3,108,662,406 was in circulation on June 1, 1909.[2]

Now, recent investigations in the subject have shown that about 85 per cent. of the business of the country is transacted by means

[1] *Monthly Summary of Commerce and Finance,* June, 1909, p. 2149.

[2] *Ibid.*

of the various forms of credit currency. It appears therefore that the total currency in circulation and in reserve at the Treasury of the country at a given time may be, approximately, $20,724,000,000, divided as follows: "standard" currency (including all notes backed by actual gold), $1,795,000,000 (about 8 per cent. of the total); government credit currency (including national-bank notes, which are backed by government bonds), $1,612,000,000 (about 7 per cent.); other credit currency—checks, drafts, bills of exchange, etc., and "credit" deposits—$17,625,000,000[3] (about 85 per cent.). In a word, of the total volume of our currency at a given time, the so-called standard currency constitutes only 8 per cent., while credit currency, in one form or another, constitutes the remaining 92 per cent. In view of these facts, it is hard to see that the issuance of a few hundred thousand or a few hundred million dollars' worth of bank-notes—based upon ample security and issued to meet the stringency as it may arise in different parts of the country—would seriously change the proportion of credits to the country's basic money. Certainly such a procedure would not make that proportion much more unhealthy than it is under normal conditions; and certainly the facts in the case are not such as to impress us strongly with the danger of producing a still greater disproportion of the aggregate liabilities of the banks of the country to the total volume of gold and silver.

The difficulty here would be cleared up considerably by the recognition of a few fundamental facts, namely: that "money," in the common conception of the term, is merely a medium of exchange; that all exchange is based ultimately upon the idea of barter; that about 85 per cent. of the business of the country is transacted already by means of credits based upon commercial security; and that, from a purely commercial standpoint, a paper dollar based upon a bushel of wheat (or two bushels of wheat) in an elevator is just as good as a paper dollar based upon 23.22 grains of gold in a bank reserve, provided, of course, that the holder of the former dollar is amply insured against loss or deterioration in the wheat.

[3] The approximations for this item and for the total circulation would be smaller if an estimate of the normal amount of cash held in reserve by banks or hoarded by individuals could have been introduced into the original calculations. The difference would not be sufficient, however, to impair the force of this comparison.

Indeed, this is the crux of the whole matter; and how far afield forgetfulness of the foregoing facts has led some of the students of the problem is indicated in the following paragraph, taken from an article by a recent writer on the subject:

> It is therefore clear that the only real money we have is our gold and the bullion value of our silver, and that in the last analysis all of the deposits of the banks—in fact all of the credits of the country—must rest upon this foundation of gold and silver.[4]

What do we mean by "real money"? I take it that the term is used here synonymously with "standard" money, that is, money made from the commodity used as the standard of value; and in this restricted sense the statement is true, so far as the reference to gold is concerned. But why include the bullion value of our silver? And if so, why not include also the bullion value of our nickel and the bullion value of our copper?

The statement that all the credits of the country must rest upon this foundation of gold and silver is untenable, it seems to me, from any standpoint. Some of the credits of the country do rest upon a foundation of gold and silver; but, as has been shown above, four-fifths of the credits of the country rest upon security growing out of the value of commodities other than gold and silver. The mere fact that we measure and express the values of these commodities in terms of gold and silver does not mean that they or the credits which may be derived from them rest upon the foundation of gold and silver. The ultimate foundation of all credit is value—some valuable thing; and this valuable thing may be wheat or cattle or land or gold or silver or anything combining the qualities of utility and scarcity.

The difficulties which have arisen from over-extended credit situations, and the serious consequences which the commercial interests of the country have had to suffer, have come, not from our failure to limit "credit" to the foundation of gold and silver, but from our failure to base it upon securities which are absolutely safe, or at least as safe as securities can be.

As a remedy for the inelasticity of our currency system, and as a device for meeting the exigencies of a time of crisis, we should

[4] *Bankers' Magazine*, July, 1909; commentary on an address delivered before the Missouri Bankers' Association by Mr. C. H. Huttig, president of the Third National Bank, St. Louis.

have an acceptable provision for an emergency circulation of bank-notes. Of course care should be taken to safeguard these notes in every way. They should be issued by the banks under the direction and supervision of the government, or by a central bank of issue, and secured by substantial commercial paper and a reasonable cash reserve. They should be limited in quantity, so as to relieve bank officials, so far as possible, of the temptation to make hazardous loans; and they should be subject to a tax which should make them unprofitable except in times of financial stringency and of consequently high discount rates, thus assuring their early redemption and retirement. Notes issued in this way could prove no possible obstacle to sound banking. They would serve not only to meet the fluctuations in the demand for cash due to seasonal variations in different sections of the country, but also to lessen, if not to obviate, the dangers arising from a general financial crisis.

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THE STRIKE AT IQUIQUE

Iquique is a port of Northern Chile on the Pacific Ocean, with a population of about 40,000. The city is built at the water's edge on a low, flat area directly under high, yellow, sand bluffs. Above the bluffs are the pampas, which stretch back in arid wastes into the interior. On these elevated plains are to be found the deposits of minerals and nitrate which have been the basis of the Chilean income since the recent war with Peru. The nitrate *officinas* are supplied with laborers mainly drawn from among the natives, or so-called *rotos*. These men have many good qualities, and are loyal and industrious when well treated; but the exploitation of the *roto* by the employing class is unfortunately not rare. In many instances the laborer is a peon, practically attached to the soil; because, by law, he cannot migrate while he is in debt to his employer and the latter is easily able to make the condition of being indebted practically permanent.

The facts as to the strike at Iquique in December, 1907, were carefully concealed from the outside world by official censorship; but its bloody outcome was an illustration, which should not go unrecorded, of the influence of a bad monetary system upon the labor question. In Chile, before the war with Peru and Bolivia